

**The Internal Revenue Service Should
Improve Procedures to Identify and
Resolve Incorrect and Missing
Taxpayer Identification Numbers**

July 1999

Reference Number: 091104



INSPECTOR GENERAL
for TAX
ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

July 30, 1999

MEMORANDUM FOR COMMISSIONER ROSSOTTI

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

This report presents the results of our review of the Internal Revenue Service's (IRS) efforts to identify and resolve tax returns filed with either incorrect or missing taxpayer identification numbers. We reviewed selected returns processed in four service centers and discussed the process with Returns Processing and Information Systems staff in the Headquarters Office.

In summary, we found some aspects of the program worked and others need improvement. The IRS should:

- Require more user involvement to ensure new computer programs work as intended.
- Study the taxpayer identification number validation system to ensure the system is programmed to properly validate taxpayer identification numbers. Modify some existing procedures to ensure returns without Earned Income Tax Credits are processed correctly when an incorrect taxpayer identification number is changed to a temporary Internal Revenue Service Number.
- Create a new computer control to identify incorrect filing status when dependents are correctly disallowed.
- Consider specialized or additional training for certain tax examiners working Revenue Protection Strategy issues and create a training module that allows examiners to correctly resolve invalid taxpayer identification numbers. Also, change some existing procedures to allow tax examiners to use taxpayer identification number information on Form 2441, Child and Dependent Care Expenses, when appropriate.

Management generally agreed with our recommendations. They revised procedures, and submitted several requests for programming changes. However, management stated that several programming changes are not scheduled to be completed before January 2000. Management attributed these delays to Information Systems staff working on Year 2000 issues and required tax law changes. We agree with management's position that the number of taxpayers potentially affected by the Year 2000 and tax law changes vastly exceeds those affected by the conditions identified in this report.

Management's response has been incorporated into the body of the report where appropriate, and the full text of their response is included as an appendix to this report. Copies of this report are also being sent to IRS executives who are affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions, or your staff may call Walter Arrison, Associate Inspector General (Wage and Investment Income Program), at (770) 455-2478.

**The Internal Revenue Service Should Improve Procedures to Identify and
Resolve Incorrect and Missing Taxpayer Identification Numbers**

Table of Contents

Executive Summary	Page	i
Objective and Scope	Page	1
Background.....	Page	1
Results	Page	2
A New Computer Program to Identify Specific Returns Did Not Work as Intended	Page	2
The System to Validate Taxpayer Identification Numbers Should Be Studied and Certain Processing Instructions Revised ..	Page	3
Internal Revenue Service Employees Need a Better Way to Recognize When a Taxpayer’s Filing Status Should Be Changed	Page	6
Improved Training on Resolving Returns With Taxpayer Identification Number Problems May Be Helpful	Page	7
Conclusion	Page	9
Appendix I – Detailed Objective, Scope, and Methodology.....	Page	10
Appendix II – Major Contributors to This Report	Page	13
Appendix III – Report Distribution List.....	Page	14
Appendix IV – Management’s Response to the Draft Report.....	Page	15
Appendix V – Head of Household (HOH) Projections	Page	25

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Executive Summary

In the past few years, the Internal Revenue Service (IRS) has attempted to reduce the number of refunds paid to persons filing fraudulent tax returns. Historically, refund fraud has involved claims for dependents or tax credits that are based on either incorrect or missing taxpayer identification numbers. The IRS has implemented a Revenue Protection Strategy (RPS) which attempts to identify returns filed with missing and incorrect taxpayer identification numbers. The objective of our audit was to determine if IRS employees identified, resolved, and correctly processed tax returns filed in 1998 with either incorrect or missing taxpayer identification numbers.

Results

For 1998, changes were to have been made to enhance the IRS' ability to identify potential problems with incorrect or missing taxpayer identification numbers. Our limited audit of the IRS' 1998 processing indicates that some computer programs, as well as employee performance, could more effectively identify and resolve incorrect and missing taxpayer identification numbers on tax returns.

A New Computer Program to Identify Specific Returns Did Not Work as Intended

In response to our prior audit, the IRS implemented a new computer program in 1998. The program was to identify taxpayers who filed a tax return in 1998, and in the prior year, with the same incorrect taxpayer identification number.

The System to Validate Taxpayer Identification Numbers Should Be Studied and Certain Processing Instructions Revised

Computer programs that match taxpayer identification numbers against two different IRS computer files produced different results and there are no computer error routines designed to identify this problem. In addition, the processing procedure should be revised to ensure returns with errors are routed to employees who have the capability to adjust the taxpayer's account.

Internal Revenue Service Employees Need a Better Way to Recognize When a Taxpayer's Filing Status Should Be Changed

We determined that another computer program, to identify taxpayers using an incorrect filing status when the qualifying dependents were properly disallowed, was not

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

implemented. We estimate the IRS lost approximately \$310,000 in revenue because some incorrect filing statuses were not changed from Head of Household to Single.

Improved Training on Resolving Returns With Taxpayer Identification Number Problems May Be Helpful

We reviewed 293 tax returns with 1 or more incorrect or missing taxpayer identification numbers. Employees correctly resolved more than one half of these returns; however, they did not make all the necessary corrections on 107 returns. This resulted in taxpayers receiving either incorrect tax assessments or incorrect notices regarding changes to the tax return.

Summary of Recommendations

The IRS should consider the following:

- Require more user involvement when testing new programs. Study and change the system for validating taxpayer identification numbers and ensure it is reliable. Also, develop additional written procedures to ensure resolution of returns with errors.
- Create and implement programming to identify tax returns with an incorrect filing status when qualifying dependents are properly disallowed.
- Consider specialized or additional training for Error Resolution employees working RPS issues. Also, change some error resolution procedures to ensure employees use information from the taxpayers' returns, as appropriate, when correcting taxpayer identification numbers.

Management's Response: Operations and Information Systems management generally agreed with our recommendations. They revised procedures and submitted several requests for programming changes. However, several programming changes are not scheduled for completion before January 2000. This is attributed to the Information Systems staff working on Year 2000 issues and required tax law changes.

Office of Audit Comment: We agree the number of taxpayers potentially affected by Year 2000 and tax law changes vastly exceeds those affected by the issues identified in this report. The complete response to this audit report is included in Appendix IV.

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Objective and Scope

The overall objective of our audit was to determine if Internal Revenue Service (IRS) employees identified, resolved, and correctly processed tax returns filed in 1998 with either incorrect or missing taxpayer identification numbers. We performed this audit from March through May 1998 in accordance with *Government Auditing Standards*. The complete management response was received in January 1999.

We conducted audit tests at the Kansas City Service Center and selected tests at the Andover, Atlanta, and Fresno Service Centers to determine if employees identified tax returns with missing taxpayer identification numbers. We also conducted tests to determine if employees correctly resolved and then processed returns originally filed with either incorrect or missing taxpayer identification numbers.

Appendix I contains the detailed objective, scope, and methodology for this review. Appendix II contains a listing of major contributors to this report.

Background

The IRS initiated the Revenue Protection Strategy (RPS) in 1995 to identify questionable returns and prevent taxpayers from filing fraudulent returns. The General Accounting Office identified filing fraud as a highly vulnerable risk area for the IRS and a Treasury task force report estimated the IRS paid about \$5 billion in refunds based on fraudulent tax returns. These tax returns usually involve erroneous exemptions and tax credits based on either missing or incorrect taxpayer identification numbers.

The Small Business Job Protection Act of 1996 (Public Law 104-188) and the Personal Responsibility and

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Work Opportunity Reconciliation Act of 1996 (Public Law 104-193) give the IRS authority to process tax returns with either missing or incorrect taxpayer identification numbers as math errors. For example, a return will be processed as a math error if the taxpayer claimed a tax credit, but did not provide a taxpayer identification number for the individual that qualified the taxpayer for the credit.

We conducted a prior audit of the IRS' math error processing during 1997. In that report, *Math Error Processing for Revenue Protection Issues* (Reference Number 083322) dated May 22, 1998, we recommended the IRS improve the use of revenue protection program resources and improve computer programming to identify and resolve these cases.

Results

We identified improvements that were needed in some computer programs to more effectively identify and resolve incorrect and missing taxpayer identification numbers. We also identified some areas where employee performance can be improved.

A New Computer Program to Identify Specific Returns Did Not Work as Intended

In response to our prior audit, IRS implemented a new computer program in 1998. The program was intended to identify taxpayers who filed a tax return in 1998, and in the prior year, with the same incorrect taxpayer identification number. Once identified, these tax returns are forwarded to the Error Resolution Unit so employees could attempt to resolve the incorrect taxpayer identification number. If they could not resolve the issue, the employees would disallow the taxpayer's personal exemption. If the taxpayer claimed an Earned Income Tax Credit (EITC), (available to certain low income working

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

taxpayers) the credit would also be disallowed. This program did not work as intended.

Shortly after the new program took effect, we identified three tax returns where the personal exemptions should have been, but were not, disallowed. Because the computer program did not identify the returns, they bypassed the Error Resolution Unit. The initial program did not work correctly due to inadequate communication and involvement by employees requesting and using the new computer program.

On April 1, 1998, we informed IRS Headquarters officials about the problem and they corrected the program by April 23, 1998.

Recommendation

1. We recommend the IRS require more user involvement in the testing process for new computer programs to ensure the test criteria produce the desired results.

Management's Response: Operations and Information Systems management will ensure joint participation in the development and documentation of computer programming changes. In addition, they will also ensure that computer programming requirements are reviewed and that walk-throughs of new requirements are made to reduce the probability of programming errors.

The System to Validate Taxpayer Identification Numbers Should Be Studied and Certain Processing Instructions Revised

Validity controls could be improved.

The IRS checks the accuracy of taxpayer name and address information on tax returns against two different computer files to ensure the validity of taxpayer identification numbers on returns. Indicator codes are then computer generated based on the information matched.

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

The Master File is the IRS' primary database of tax return information. The Entity Index File is comprised in part of names and addresses of taxpayers who file tax returns at that service center.

Computer validity checks ensure valid taxpayer identification numbers are used.

Returns with correct taxpayer identification numbers post to the "valid" side of the Master File. Returns with incorrect or temporary numbers post to the "invalid" side.

One indicator shows the taxpayer identification number, name, and address are on both the Master File and the Entity Index File. The other indicator shows there is no record of the taxpayer on the Entity Index File. Both of the indicators should not be present on the same return.

We identified 59 tax returns where both indicators were present. In eight cases, the taxpayers did not have tax accounts on the Master File, and they filed the tax returns with incorrect taxpayer identification numbers. These returns bypassed an error resolution system where the primary exemption and EITC would have been disallowed, if applicable. The eight tax returns were sent to the Unpostable Unit so employees could resolve problems created when transactions do not meet computer validity checks. The employees took the appropriate actions on seven of the eight tax returns.

Computer error check routines to identify this combination of indicators as a potential problem have not been established. We estimate that approximately 2,950 tax returns (processed at 1 service center during 1 week) had both indicators, and 400 of these tax returns had incorrect taxpayer identification numbers.¹

Modifying Unpostable Procedures Would Strengthen the Revenue Protection Strategy

Tax return processing guidelines were revised as a result of our prior audit. The revised guidelines are adequate for tax returns claiming the EITC. However, if this tax credit is not involved, the tax return will be allowed to post to the invalid side of the Master File and the account will be coded to prevent refund issuance. The tax law requires the IRS to disallow a taxpayer's personal tax exemption if an incorrect taxpayer identification number is used.

¹ Based on projections against our 2 percent sample of 11,864: $59 \div .02 = 2950$; $8 \div .02 = 400$.

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Routing returns to another unit would allow more thorough corrective actions.

We identified 38 tax returns where taxpayers used an incorrect taxpayer identification number and did not claim the EITC. The personal exemption amounts on these returns should have been, but were not, disallowed.

Unpostable Unit employees changed 8 of the 38 returns to temporary numbers used by the IRS for processing purposes. While the employees' actions allowed them to continue with processing, the employees did not resolve the personal exemption issue. The employees did not disallow the exemptions because they did not have the capability to adjust the account. As a result, the taxpayers did not receive the proper notice and they may be unaware of the need to correct their taxpayer identification numbers. A better course of action would be to route the returns to employees in another unit, who do have the capability to disallow the personal exemption.

Recommendations

2. We recommend a study of the taxpayer identification number validation system to ensure indicators are reliable. Specifically, ensure indicator codes properly identify all incorrect taxpayer identification numbers.

Management's Response: Information Systems management will work with Submission Processing and Customer Service management in the Office of the Chief Operations Officer organization to analyze the need to conduct a study, analyze alternatives, and institute changes if necessary.

3. We also recommend the Unpostable Unit develop additional procedures to send all tax returns with either incorrect or IRS temporary identification numbers, but not claiming the EITC, to the Reject Unit.

Management's Response: Unpostable procedures are being revised to send all tax returns with incorrect taxpayer identification numbers to the Reject Unit for processing. The new Internal Revenue Manual procedures are scheduled to be in the field by January 1999.

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Internal Revenue Service Employees Need a Better Way To Recognize When a Taxpayer's Filing Status Should Be Changed

In 1997 and 1998, the IRS incorrectly allowed taxpayers to use the Head of Household filing status even though the dependents they claimed were correctly disallowed during routine tax return processing. Employees are to disallow the dependents shown on tax returns when the dependents' taxpayer identification numbers are either incorrect or missing. The employees are also supposed to change the taxpayers' filing status to Single.

Filing status and dependent exemptions were not always worked correctly.

We identified 1,106 tax returns in 2 IRS service centers where all dependents were disallowed because of either incorrect or missing taxpayer identification numbers. However, the taxpayers' filing status was not changed from Head of Household to Single. We reviewed a sample of 40 of these tax returns and determined the dependents were correctly disallowed on 34 tax returns, but the filing status was not changed. We also determined that in five instances dependents claimed were inappropriately disallowed. In the remaining instance, a qualifying dependent was listed elsewhere on the return.

Based on our sample results, we estimate the IRS lost approximately \$310,000 in revenue by not properly changing the filing status on 946 tax returns filed during 3 weeks of processing. Using the same sample, we estimate that the IRS inappropriately disallowed dependents on 142 tax returns at the 2 service centers (see Appendix V).

Additionally, we reviewed the notices sent to the 40 taxpayers explaining why their tax return information was changed. We found that 28 taxpayers received incorrect notices.

We identified this same issue in our prior audit. In response to that audit report, the IRS agreed to develop a new computer program that would identify these returns. However, IRS programmers will not be able to complete the necessary programming until January 2000.

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Recommendation

4. To protect revenue and ensure the correct tax is assessed, a new computer control should be implemented as soon as possible to identify for the Error Resolution Unit those tax returns claiming Head of Household filing status and no dependents.

Management's Response: A new computer control has been re-requested to ensure Error Resolution employees take a second look at tax returns claiming Head of Household filing status where all dependents claimed were disallowed, but the filing status was not changed. This change was previously requested for implementation in January 1999, but was not acted upon due to Information Systems resource issues. A new implementation date is planned for January 2000. Until that time, additional emphasis will be given to this issue during employee training.

Improved Training on Resolving Returns With Taxpayer Identification Number Problems May Be Helpful

We reviewed 293 tax returns with 1 or more incorrect or missing taxpayer identification numbers. The Error Resolution employees correctly resolved more than one half of these returns; however, they did not make all the necessary corrections on 107 returns.

The incorrect resolution of taxpayer identification numbers caused several problems for the IRS. First, 52 of 107 taxpayers (49 percent) received incorrect tax assessments. Thirty-two of these taxpayers were under assessed \$42,622 and 20 were over assessed \$15,617.

Secondly, 77 taxpayers received incorrect notices regarding changes made to their tax returns. In these cases, taxpayers either did not receive notices alerting them to problems on their returns or they received information explaining actions that the IRS should not

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

have taken. The issuance of incorrect notice information was generally caused by Error Resolution employees incorrectly resolving the account.

A training system might be the cause of some errors.

We could not link these problems to any single cause. We did find, however, that employees did not always follow procedures to revalidate corrected taxpayer identification numbers. The failure to revalidate the numbers might be directly related to a systemic deficiency in the core training program. Error Resolution employees are required to “Clear” certain error conditions when confronted with them in training modules. It is possible the errors are occurring simply because employees have learned the habit of clearing the error conditions.

We also determined that employees have another source of taxpayer identification number information available to help them resolve these problems. Form 2441, Child and Dependent Care Expenses, contains taxpayer identification numbers for children claimed. By changing work procedures to allow Error Resolution employees to validate and use this information, IRS might more easily resolve some of the existing taxpayer identification number problems and might not need to conduct additional research to find a correct taxpayer identification number.

Recommendations

5. To assist in reducing procedural errors, the IRS should develop specialized training and create a training module that allows Error Resolution employees to correctly resolve incorrect taxpayer identification number problems.

Management’s Response: Increased emphasis on taxpayer identification number issues will be incorporated into Error Resolution employee training in 1999. A training module will not be considered until January 2000 because Information Systems resources are reserved for legislative changes.

6. We also recommend Error Resolution employees be instructed to use and validate taxpayer identification

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

number information on Form 2441, Child and Dependent Care Expenses. This could be done by changing work procedures.

Management's Response: The Error Resolution Unit work procedures have been revised to instruct Error Resolution employees to check Form 2441 and Form 8814, Parent's Election to Report Child's Interest and Dividends, to perfect name and taxpayer identification number information. The new procedures are scheduled to be in the field by January 1999. Computer programming changes for the validation of taxpayer identification number data entered by Error Resolution employees are being submitted for January 2000 implementation.

Conclusion

Our audit indicates that a computer program and system to identify certain returns for correction, as well as some procedures, did not work as planned. Specifically, a computer program to identify instances where taxpayers filed returns using an incorrect taxpayer identification number in multiple years did not work. Also, a system to validate taxpayer identification numbers did not work and some returns bypassed some review processes. We also determined that procedures should be changed to ensure that employees with the proper authority and capability receive and resolve certain returns with errors.

Further, we determined that in some cases the filing status of some taxpayers was not properly changed, resulting in an estimated revenue loss of approximately \$310,000. In other cases, taxpayers were under assessed \$42,622 and others over assessed \$15,617. Many did not receive notices alerting them to the problem.

We believe the IRS can better fulfill its Revenue Protection Strategy by implementing our recommendations.

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of our audit was to determine if Internal Revenue Service (IRS) employees identified, resolved, and correctly processed tax returns filed in 1998 with either incorrect or missing taxpayer identification numbers.

Objective 1: To determine if Code and Edit Unit employees properly identified tax returns that did not have taxpayer identification numbers for taxpayers, their spouses, and/or their dependents, we:

1. Identified 50 tax returns (from a 2 percent sample of tax returns processed at the Kansas City Service Center) on which the taxpayer claimed the Earned Income Tax Credit (EITC) or Child and Dependent Care Credit. Two tax returns met our criteria (missing taxpayer identification numbers) and we reviewed them to determine if employees identified all missing taxpayer identification numbers.
2. Identified 81 tax returns which were coded as missing primary, secondary, dependent, or EITC qualifying child taxpayer identification numbers. We reviewed 44 tax returns to determine if employees identified all missing taxpayer identification numbers.
3. Reviewed 46 tax returns with selected notices to determine if taxpayers received notices that properly described all taxpayer identification number problems on their tax returns.
4. Reviewed 29 tax returns at the Kansas City Service Center on which a Child and Dependent Care Credit was claimed and no dependents were shown living at home. We also reviewed revised Internal Revenue Manual guidelines and training manual changes to determine if they were adequate.
5. Reviewed 25 tax returns with a Form 2441, Child and Dependent Care Expenses, that were identified at the Kansas City Service Center. We also followed up on the status of programming changes that require transcribing and validating provider names and taxpayer identification numbers, and that create a code identifying incorrect taxpayer identification numbers.

Objective 2: To determine if Error Resolution employees properly resolved those conditions where taxpayers either failed to provide taxpayer identification numbers or where taxpayers provided incorrect numbers for themselves, their spouses, and/or dependents, we:

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

1. Reviewed 50 tax returns (from a 2 percent sample of tax returns processed at the Kansas City Service Center) to determine if Error Resolution employees properly disallowed exemptions and credits for Child and Dependent Care and/or Earned Income.
2. Reviewed 64 tax returns identified as missing primary, secondary, dependent, or EITC qualifying children taxpayer identification numbers to determine if employees properly disallowed the respective exemption(s) and/or EITC.
3. Reviewed 41 tax returns identified as having incorrect primary, secondary, dependent or EITC qualifying children taxpayer identification numbers to determine if Error Resolution employees properly disallowed primary and dependent exemptions and credits for Child and Dependent Care and/or Earned Income.

Because we found indicator codes on returns in combinations that should not have occurred, we expanded our audit test and:

- a. Queried 173,026 return records from a 2 percent sample of tax returns processed during 2 weeks at the Andover, 1 week at the Fresno, and 12 weeks at the Kansas City Service Centers.
 - b. Queried 11,864 return records from a 2 percent sample of tax returns processed during 1 week at the Kansas City Service Center. Reviewed 59 accounts to determine if the codes reflected tax account information.
 - c. Identified and reviewed three tax returns filed with incorrect taxpayer identification numbers that appeared to have incorrect indicator codes.
4. Reviewed 106 tax returns to determine if the taxpayer received a notice that described all taxpayer identification number problems on the return.
 5. Reviewed 25 tax returns to determine if the correct computer field was properly used to disallow dependent exemptions and if taxpayers received correct notices. We also evaluated the adequacy of processing instructions and the status of programming changes, which were submitted to update this process.
 6. Reviewed 40 tax returns identified at the Atlanta and Kansas City Service Centers as having either incorrect or missing dependent taxpayer identification numbers. We reviewed the tax returns to determine if the correct computer field was used to disallow dependents and the filing status was changed from Head of Household to Single, and to determine if taxpayers received correct notices. We reviewed 5 of the 40 tax returns for other taxpayer identification number issues to determine if they were resolved correctly. We also followed up on the status of the request for programming changes to create a new computer code for this condition.
 7. Reviewed four tax returns where the primary taxpayer identification number was a temporary number, an unissued social security number, or a number associated with

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

either resident or non-resident alien taxpayers to determine if the EITC was properly disallowed and if taxpayers received correct notices. We also reviewed processing instructions to determine if they were adequate.

8. Reviewed 92 tax returns identified at the Atlanta, Andover, and Kansas City Service Centers to determine if employees were selecting the correct notice for taxpayer identification number problems. We also determined if training material was adequate.

Objective 3: To determine if the service center programs ensured that valid taxpayer identification numbers for dependents and EITC qualifying children were present, we:

1. Reviewed 10 tax returns identified at the Kansas City Service Center as missing taxpayer identification numbers for the EITC qualifying children.
2. Reviewed 41 tax returns identified as having no information in certain required fields to determine if taxpayer identification numbers were validated before amounts for exemptions and credits for Child and Dependent Care and/or Earned Income were allowed. We also determined if taxpayers received correct notices.
3. Reviewed three tax returns identified at the Andover and Kansas City Service Centers as having blanks in two fields to determine if EITC children's taxpayer identification numbers were validated when employees subsequently received a missing EITC schedule and if taxpayers received correct notices. We also followed up on the status of the request for programming changes to the revalidation process.

**The Internal Revenue Service Should Improve Procedures to Identify and
Resolve Incorrect and Missing Taxpayer Identification Numbers**

Appendix II

Major Contributors to This Report

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**The Internal Revenue Service Should Improve Procedures to Identify and
Resolve Incorrect and Missing Taxpayer Identification Numbers**

Appendix III

Report Distribution List

Deputy Commissioner for Operations C:DO
Chief Operations Officer OP
Chief Information Officer IS
Assistant Commissioner (Forms and Submission Processing) OP:FS
Assistant Commissioner (Program Evaluation and Risk Analysis) M:OP
National Director, Submission Processing OP:FS:S
Director Corporate Processing Division IS:S:CP
Executive Officer for Service Center Operations OP:SC
Office of Management Controls M:CFO:A:M
National Director for Legislative Affairs CL:LA
Regional Commissioners
Service Center Directors

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Appendix IV

Management's Response to the Draft Report



ASSISTANT COMMISSIONER
(FORMS AND SUBMISSION
PROCESSING)

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

October 22, 1998

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9400121
Inspector

MEMORANDUM FOR CHIEF INSPECTOR

THRU:

John M. Dalrymple
John M. Dalrymple
Chief Operations Officer

FROM:

Brien T. Downing *Brien T. Downing*
Assistant Commissioner
(Forms and Submission Processing)

SUBJECT:

Draft Internal Audit Report - Effectiveness of Math Error Processing for Identifying and Resolving Invalid and Missing Taxpayer Identification Numbers (980023)

Thank you for the opportunity to review the subject draft Internal Audit report. We have responded to all recommendations except Recommendation 2. A separate memorandum will be issued by the Office of the Chief Information Officer in response to Recommendation 2.

Recommendation #1

We recommend that the Service require more user involvement in the testing process for new National Accounts Profile (NAP) programs to ensure the test criteria produce the desired results.

Assessment of Cause(s)

Three returns were filed with invalid Taxpayer Identification Numbers (TINs) that were not identified as matching the invalid side of Master File (MF). The primary exemptions were not disallowed as a result of the invalid TINs. The NAP Access Indicator "I" was supposed to be set when a taxpayer's primary TIN and name control matched data on the invalid side of MF. This program error adversely impacted a new error code (EC 005). This error code causes these returns to be sent to the Error Resolution System (ERS) for a search for a valid account and if not located, for disallowance of the primary exemption and the claim for Earned Income Credit (EIC).

Corrective Actions

Once this was brought to the attention of the National Office, a Request for Information Services (RIS) (TSF-8-0141) was prepared and implemented to correctly set the NAP

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

2

Access Indicator "I" to identify data on the invalid side of the MF. We will ensure that Joint participation in RIS discussions, review of Functional Specification Packages, and walk-throughs of new requirements take place to reduce the probability of program glitches like this in the future.

Implementation Date

Completed: April 23, 1998

Responsible Officials

Chief, Paper Submissions Branch
National Director, Submission Processing
Assistant Commissioner (Forms and Submission Processing)

Recommendation #3 *Please reword the recommendation to say:*

We also recommend that the Unpostable Function develop additional procedures to route all returns without EIC to the Reject Function when an invalid TIN is present or is changed to an Internal Revenue Service Number (IRSN).

Assessment of Cause(s)

The current Unpostable processing guidelines are not adequate to ensure that all returns with invalid primary TINs are properly resolved. Only those returns with invalid primary TINs and EIC are routed to the Reject Function for resolution of the invalid TIN condition. If EIC is not involved, the Unpostable Function posts the return with an invalid primary TIN to the invalid side of the Individual Master File (IMF).

Corrective Actions

Procedures are currently being revised in the Unpostable Function's Internal Revenue Service Manuals (IRM) 3.12.179 and 3.13.222 to send all invalid TINs to the Reject Unit for processing. The IRMs, currently in the clearance process, are scheduled to be in the field January 1, 1999.

Implementation Date

Proposed: January 1, 1999

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

3

Responsible Officials

Chief, Paper Submissions Branch
National Director, Submission Processing
Assistant Commissioner (Forms and Submission Processing)

Recommendation #4

To protect revenue and ensure the correct tax is assessed, a new error code should be implemented as soon as possible to identify returns with a Head of Household filing status when no dependents are claimed.

Assessment of Cause(s)

In some instances, ERS examiners disallowed all dependents for either invalid or missing SSN conditions, but did not change the filing status from Head of Household to Single.

Corrective Actions

A RIS (TSF-9-0070) is in the process of being re-submitted for January 3, 2000, implementation, requesting a new error code (EC 034). The ERS IRM procedures currently require the tax examiner to make the adjustment to the filing status when working Error Codes related to dependent TINs. This new Error Code will ensure ERS examiners take a second look at returns claiming Head of Household filing status where all dependents claimed were disallowed during the ERS processing, but the filing status was not updated. Returns with the Head of Household filing status that claim no dependents will also fall out under this error code for a check to see if a child is identified on Line 4 of the tax return. This change was previously requested for January 1, 1999, implementation, but was not acted upon due to IS resource issues. In addition, increased emphasis will be made during ERS training (see Recommendation 5 below).

Implementation Date

Proposed: January 3, 2000

Responsible Officials

Chief, Paper Submissions Branch
National Director, Submission Processing
Assistant Commissioner (Forms and Submission Processing)

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

4

Recommendation #5

To assist in reducing procedural errors, the Service should develop specialized training and create a NAP training module that allows ERS examiners to correctly resolve invalid TIN conditions when working math error issues.

Assessment of Cause(s)

ERS examiners did not correctly resolve invalid or missing TIN conditions.

Corrective Actions

- (a) Agreement has been reached with the course developers, to provide increased emphasis on TIN issues during ERS training.
- (b) IS has limited programming resources available due to Y2K programming needs. These resources are reserved for legislative changes; therefore, discretionary requests were withdrawn from consideration.

Implementation Date

- (a) Proposed: January 1, 1999
- (b) Proposed: January 3, 2000

Responsible Officials

Chief, Paper Submissions Branch
National Director, Submission Processing
Assistant Commissioner (Forms and Submission Processing)

Recommendation #6

We also recommend ERS examiners be instructed to use NAP to validate Social Security Number (SSN) information on Form 2441 (Child and Dependent Care Expenses). This could be accomplished by changing IRM procedures for both EC 010 and 012.

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

5

Assessment of Cause(s)

A number of errors occurred because ERS examiners did not revalidate dependent or EIC qualifying child SSN when re-inputting corrected SSN information.

Corrective Actions

- (a) The ERS IRM 3.12.3 procedures have been revised to include instructions for ERS examiners to check the Form 2441 and Form 8814 (Parent's Election to Report Child's Interest and Dividends), to perfect name and TIN information. The IRM is in the clearance process and is scheduled to be in the field by January 1, 1999.
- (b) A RIS (TSF-9-0070) is in the process of being submitted for January 3, 2000, implementation, requesting NAP revalidation of data that has been entered by ERS tax examiners.

Implementation Date

- (a) Proposed: January 1, 1999
- (b) Proposed: January 3, 2000

Responsible Officials

Chief, Paper Submissions Branch
National Director, Submission Processing
Assistant Commissioner (Forms and Submission Processing)

If there are any questions, please have your staff call my Internal Audit liaison, Cris Balzereit, at (202) 622-7055.

**The Internal Revenue Service Should Improve Procedures to Identify and
Resolve Incorrect and Missing Taxpayer Identification Numbers**



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

JAN 15 1999

MEMORANDUM FOR CHIEF INSPECTOR

FROM: *for* David W. Junkins *M. D. Junkins*
Director, Office of Information Resources Management IS:IR

SUBJECT: Management Response to Internal Audit Draft Report -
Effectiveness of Math Error Processing for Identifying and
Resolving Invalid and Missing Taxpayer Identification Numbers
(980023)

The Assistant Commissioner for Systems Development has reviewed the subject draft internal Audit Report. The management response is attached.

If you have any questions, please call me on (202) 283-4060, or have a member of your staff call Donna Downing on (202) 283-4159.

Attachment

cc: Assistant Chief Inspector (Internal Audit)
Deputy Director, Office of Audit Projects

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Response to Draft Internal Audit Report -- Effectiveness of Math Error Processing for Identifying and Resolving Invalid and Missing Taxpayer Identification Numbers

Recommendation #2

We recommend a study of the overall National Account Profile (NAP) validation process be made to ensure NAP indicators are reliable. Specifically, we recommend that NAP programming be changed to ensure Response Indicators identify all invalid primary Taxpayer Identification Numbers (TINs).

Assessment of Cause

To date, NAP indicators have proven to be a reliable source of information for an account at Master File. NAP validations have provided a valuable function to the Service by providing "up-front" validity checks. However, Internal Audit has reported several occurrences of invalid combinations of NAP indicators present at the point of Master File posting. Subsequent to the issuance of the above referenced report by Internal Audit, testing continued by the developers/programmers in an attempt to recreate some of the erroneous combinations reported by the Internal Audit document. Throughout testing, the NAP validation programs consistently produced the expected combinations of the NAP indicators. The NAP validation programs have not produced any of the erroneous combinations that were reported by Internal Audit. In addition, these erroneous combinations were never reported by our Systems Acceptability Test (SAT) counterparts. It is our belief that the NAP validation programs are setting the correct values for the NAP indicators, and that they continue to be a reliable source of information for Master File validity checks.

While the NAP validation process is accurate and reliable, it must be noted that the indicators set during NAP validation may be subsequently changed within Pipeline Processing, and therefore may have been altered before reaching Master File for posting. A variety of combinations of the NAP-EIF-RESPONSE-CD and the NAP-ACCESS-CD have been provided to the NAP section for review/comment. Without tracking each individual case throughout the Pipeline, it is virtually impossible to state exactly what happened with each individual return. However, due to procedures inherent in the Mainline Processing, there are several plausible explanations for the combinations ultimately reviewed by Internal Audit. These explanations are included below.

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Response to Draft Internal Audit Report -- Effectiveness of Math Error Processing for Identifying and Resolving Invalid and Missing Taxpayer Identification Numbers

- (1) Combinations of NAP-ACCESS-CD equal to "2" (TIN not found) but "S" (All matches) in the NAP-EIF-RESPONSE-CD:

Reference IA draft report statement, pg. 5:

"We determined the NAP Access Indicator "2" or the NAP/EIF Response Indicator "S" contradicted tax account information."

It has been verified that occurrences of the 2,S combination have appeared as a result of the AUTOTIN correction process within Mainline Processing. The AUTOTIN correction process was implemented as a result of RIS #RPA-2-0423, requested by Internal Audit. During the AUTOTIN correction process, an invalid TIN may be changed or corrected to a valid TIN through research against the Name Search Facility (NSF). Subsequently, the corrected TIN is validated within the GMFCK program, which follows the AUTOTIN correction. The results of the GMFCK validation against the NAP are returned in the GMFCK output file (the GMFNAP01 file), which is then input to the GMF37 program.

Within the GMF37 program, the original NAP-EIF-RESPONSE-CD resulting from early NAP validations, such as from within the Distributed Input System (DIS), is replaced with the NAP-EIF-RESPONSE-CD returned from the GMFCK validation program. However, the GMF37 program does NOT replace the original NAP-ACCESS-CD from the earlier validations. This results in combinations such as the "2" in the NAP-ACCESS-CD (indicating that the TIN was not located on the original NAP access) and the "S" in the NAP-EIF-RESPONSE-CD (indicating that the TIN/name control matched at the NAP subsequent to the AUTOTIN correction).

- (2) Combinations with value zero in the NAP-ACCESS-CD (usually meaning "NAP not accessed") yet a value other than blank in the NAP-EIF-RESPONSE-CD.

If the validation was done via DISCK, the NAP would set such combinations as "S" in the NAP-EIF-RESPONSE-CD, and leave the blank (our initialized field) in the NAP-ACCESS-CD. DIS programs, on the other hand, initialize their NAP access fields at zero. If blanks are returned from the NAP in either indicator, the blank is ignored and the initial value of zero that was set by DIS remains. This results in combinations such as 0,S or 0,D.

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Response to Draft Internal Audit Report -- Effectiveness of Math Error Processing for Identifying and Resolving Invalid and Missing Taxpayer Identification Numbers

- (3) Miscellaneous invalid combinations of NAP indicators - possible areas where a discrepancy may occur between the NAP indicators and the associated entity information:
- (A) Once the TIN and name control have been verified at the NAP, the return is "key verified." DIS operators who key verify the return may change the TIN and/or name control on the return. However, the NAP is not reaccessed for verification. This means that the original indicators set through the DISCK program will remain in the record with different entity information than what originally was validated. This could cause incorrect NAP indicators to appear and may cause error codes going to ERS to be set or not be set erroneously.
 - (B) When Block Out of Balance (BOB) correction takes place, a missing return may be added, but it is not verified against the NAP at this point. If an existing return is corrected at this point, Section 01 of the Work Record may be replaced with new entity information, including the TIN and name control information. However, the BOB correction programs do not recognize if/when the SSN is changed, so the original NAP indicators remain in the record and are not overlaid with blanks. Again, this could result in entity information that may not be related to the indicators in the same record.
 - (C) Individual Master File (IMF) Document Specific processing will check to see if the NAP was not accessed, possibly due to a telecommunications problem, by looking for blanks in both indicators. However, due to the fact that these blanks would be disregarded by DIS, and zeroes remain - these returns will not go to ERS for additional validations. It is possible that a number of returns with invalid name/TIN combinations got through the system due to these types of errors where the NAP was not actually even accessed.

In summary, although the NAP validation process is accurate, there are many hands that may touch the NAP indicators throughout Mainline Processing and alter the values from their initial settings. The NAP-EIF-RESPONSE-CD can be altered from its original setting as a result of the AUTOTIN correction process. Also, the DIS processing will carry zeroes in the NAP indicators in lieu of any blanks set by NAP processing. In addition, the key verification and BOB processing may change entity information, without revalidating the changed TIN and/or name control against the NAP. Without revalidation of the TIN/name control after such changes, NAP indicators may no longer

The Internal Revenue Service Should Improve Procedures to Identify and Resolve Incorrect and Missing Taxpayer Identification Numbers

Response to Draft Internal Audit Report -- Effectiveness of Math Error Processing for Identifying and Resolving Invalid and Missing Taxpayer Identification Numbers

correctly reflect the validity of the entity information remaining at the time of Master File posting. Finally, invalid TIN/name control combinations can still exist at the time of Master File processing, due to the fact that because of telecommunications problems, the entity information was never successfully NAP validated.

Corrective Action for Recommendation #2

Information Systems (IS) will work with Submission Processing and Customer Service in the Chief Operations Officer organization to:

- 1) analyze current processes, problems, and programs to determine the need for a study,
- 2) analyze alternatives for processes and systems redesign if necessary, and
- 3) agree on approaches and have RISs issued as appropriate by COO if it is determined that changes need to be made.

If there are significant resource commitments, the issue may need to be brought before the Taxpayer Treatment and Service Improvements (TTSI) Executive Steering Committee (ESC).

Implementation Date:

Completed: _____

Proposed: **10/01/99**

Responsible Official:

Chief Information Officer IS
Deputy Chief Information Officer (Systems) IS
Assistant Commissioner for Systems Development IS:S
Director, Submission Processing Division IS:S:SP

**The Internal Revenue Service Should Improve Procedures to Identify and
Resolve Incorrect and Missing Taxpayer Identification Numbers**

Appendix V

Head of Household (HOH) Projections

	Center A	Center B	Total	
Number of returns	928	178		1106
Number of returns reviewed	30	10	40	
Number of returns w/HOH issue	26	8	34	
% of returns where HOH issue identified	$(26/30) = .8667$	$(8/10) = 0.8$		
Tax effect of returns w/HOH issue	\$9,188.00	\$1,425.00		
Average tax effect of returns w/HOH issue	\$353.38	\$178.13		
Estimated number of returns w/HOH issue	$(928 \times .8667) = 804$	$(178 \times .80) = 142$		946
Estimated revenue loss due to HOH issue	$(804 \times \$353.38) = \$284,118.00$	$(142 \times \$178.80) = \$ 25,390.00$		\$309,508
Number of returns where dependents were inappropriately disallowed	4	1	5	
% of returns where dependents were inappropriately disallowed	0.1333	0.1		
Estimated number of returns where dependents were inappropriately disallowed	$(928 \times .1333) = 124$	$(178 \times .10) = 18$		142
Number of returns where qualifying child listed on Line 4 of return	0	1	1	